Note to : Mr. Keith Dunt

Tobacco Strategy Group

I enclose extracts from the minutes of the TSG meeting held on 2nd December 1992 of the items for which you were present.

H.C. Barron

HCB/djs
11th December 1992

Enclosure

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Tobacco Strategy Group

A meeting of the Tobacco Strategy Group was held on Wednesday, 2nd December, 1992.

30. Andean Pact: Mr Dunt made a presentation on the opportunities for BAT in the Andean Pact territories. He reported that Venezuela and Colombia are moving faster than Ecuador, Bolivia and Peru to lower tariffs. In his opinion the Andean Pact Common Market will only be operational in the medium term between Venezuela and Colombia, with a subsequent agreement being signed with Mexico as a further step in the G3 grouping. As BAT has a company in Venezuela, the main immediate focus for the Group must be Colombia. The Colombian market is by far the largest in the Andean Pact at 31.2bn and a very high proportion is Duty Not Paid. BAT has a near 10% market share in the Andean Pact net of Venezuela, PM 13% and local manufacturers 77%. This market share presence can be improved upon. The possibilities of acquiring either Protabaco in Colombia or El Progreso in Ecuador are a secondary priority after focusing the Group's brand portfolio and efforts in a more concerted fashion.

31. It was agreed that:
- the approach to the Andean Pact markets must be brand/market driven not manufacturer driven;
- the brand portfolio needs to be more focused: High price - Lucky Strike, Kent, Kool; Medium price - Hollywood, Belmont, Viceroy; Low price - Minister, and Consul if necessary;
- the trademark problems must be resolved. The action being taken is endorsed;
- the group manufacturers must share a common infrastructure;
- one person must be accountable for the Colombian market. A joint proposal is to be made to the next TSG meeting supported by BATCo, Brown & Williamson and Souza Cruz.

32. Mercosul/Uruguay: The possible acquisition of Monte Paz in Uruguay was discussed. It was agreed that BAT did not need the manufacturing capacity (the closure of which might cause political problems) and therefore what would be bought is local brands and distribution. Citibank valued the business at $55m assuming the continuation of current profit levels and including Leaf inventory and a printing company that are not needed. The value of the business should be recalculated in the light of Mercosul and compared with increasing exports of BAT's own brands into Uruguay. Monte Paz owns many Souza Cruz brands in Uruguay. It is not yet clear whether they will be able to export these brands from Uruguay to Brazil within Mercosul. If this is possible it will be a real threat to Souza Cruz.

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33. Booz Allen made recommendations about rationalisation opportunities between Souza Cruz and Nobleza-Piccardo. Task forces have been set up to validate the figures behind these recommendations. There are opportunities to sell Souza Cruz brands in Argentina and Nobleza-Piccardo brands in Brazil, but it is a higher priority for both companies to address the challenge from Philip Morris. The unsatisfactory trademark position is being worked on. A progress report will be made to the TSG meeting in May 1993.

34. NAFTA: Mr Pritchard reported that NAFTA is expected to come into force on 1st January 1994 as scheduled. The US and Mexican negotiators reached agreement on the cigarette rule of origin which requires that the cost of offshore tobacco including oriental not exceed 9% of the declared export value. Even with the 50% tariff (declining gradually to zero over 10 years), B&W export cigarettes should be able to compete with the premium brands in Mexico. However it is a large market and early entry and considerable investment will be needed, therefore it is not expected that significant profits will be made for eight or nine years. Mr Sandefur will report to the next TSG meeting on the preparations being made by B&W.

35. Mr Mercier pointed out that the trademark position needs to be resolved as ITL owns the Marlboro, Lucky Strike and Pall Mall brands in Canada. Mr Brown pointed out that there could be an opportunity for ITL to manufacture BAT trademarks for Mexico since it is in NAFTA but not in the US. A possible longer term threat may be that, under Mexican law, a manufacturer who owns a trademark in Mexico may export a product to any country. Mr Pritchard will report on the position with respect to intellectual property rights within NAFTA and Mr Bramley on trademarks in US/Canada/Mexico at the next TSG meeting.

10th December 1992

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